

**BEFORE THE
CALIFORNIA BOARD OF ACCOUNTANCY
DEPARTMENT OF CONSUMER AFFAIRS
STATE OF CALIFORNIA**

In the Matter of the Accusation Against:)

BRADLEY JAMES SCHMIDT)
CPA License No. 69363)

Respondent.)
_____)

Case No. AC-2005-1
OAH No. N2005010414

DECISION AFTER NONADOPTION

This matter came on regularly for hearing before Denny R. Davis, Administrative Law Judge of the Office of Administrative Hearings on March 30, 2005. Complainant was represented by Kent D. Harris, Deputy Attorney General. Respondent appeared and represented himself. Oral and documentary evidence was presented and the record was closed and the matter was submitted.

The Administrative Law Judge issued his Proposed Decision on May 3, 2005. The Proposed Decision of the Administrative Law Judge was not adopted by the California Board of Accountancy ("Board"). On June 8, 2005, the Board issued an Order of Nonadoption. On June 14, 2005, the Board issued its "Notice of Receipt of Transcripts and Exhibits."

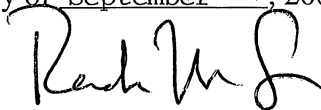
Having reviewed the record in its entirety including the transcript and written argument submitted by both parties, the Board now makes and enters its Decision After Nonadoption as follows:

ORDER

The California Board of Accountancy hereby adopts the attached Proposed Decision dated May 3, 2005, as its decision in this matter.

This decision shall become effective on October 21, 2005.

IT IS SO ORDERED this 21st day of September, 2005.



Renata M. Sos, President
FOR THE CALIFORNIA BOARD OF ACCOUNTANCY
DEPARTMENT OF CONSUMER AFFAIRS

BEFORE THE CALIFORNIA BOARD OF ACCOUNTANCY
DEPARTMENT OF CONSUMER AFFAIRS
STATE OF CALIFORNIA

In the matter of the Accusation
against:

BRADLEY JAMES SCHMIDT
4591 East Calle Redonda
Phoenix, AZ 85018

Certified Public Accountant
License No. 69363

Respondent

Case No.: AC-2005-1

OAH No.: N2005010414

ORDER OF NONADOPTION OF PROPOSED DECISION

Pursuant to Section 11517 of the Government Code, the Proposed Decision of the Administrative Law Judge in the above-entitled matter is not adopted. The California Board of Accountancy will decide the case upon record, including the transcript of the hearing held on March 30, 2005, and upon such written argument as the parties may wish to submit. The parties will be notified of the date for submission of such argument when the transcript of the above-mentioned hearing becomes available.

IT IS SO ORDERED this 8th day of June, 2005



Renata M. Sos
Board President

BEFORE THE
CALIFORNIA BOARD OF ACCOUNTANCY
DEPARTMENT OF CONSUMER AFFAIRS
STATE OF CALIFORNIA

In the Matter of the Accusation Against:

BRADLEY JAMES SCHMIDT
4591 East Calle Redonda
Phoenix, AZ 85018

Certified Public Accountant Certificate
No. 69363

Respondent.

Case Number AC- 2005-1

OAH No. N2005010414

DECISION

On March 30, 2005, in Sacramento, California, Denny R. Davis, Administrative Law Judge, Office of Administrative Hearings, State of California, heard this matter.

Kent D. Harris, Deputy Attorney General, represented the complainant.

Bradley James Schmidt, respondent, represented himself.

Evidence was received, the record was closed and the matter was submitted on March 30, 2005. All pre-hearing jurisdictional requirements have been met. Jurisdiction for this proceeding does exist.

FACTUAL FINDINGS

1. Complainant, Carol Sigmann, Executive Officer of the California Board of Accountancy, filed the Accusation against respondent in her official capacity only and not otherwise.

2. The Board issued to respondent Certified Public Accountant Certificate Number 69363, on July 21, 1995. The certificate was renewed and remained in active status except from April 1, 1999, through April 30, 2000, when for nonpayment of fees the certificate was delinquent. The certificate was renewed then expired again for failure to pay fees. It was renewed in an inactive statue through March 31, 2005.

3. Respondent was employed by the Arthur Andersen firm in 1994. After serving in the Los Angeles office for one year he was transferred to the Phoenix, Arizona office where he became an Audit Senior. In that capacity he participated in an audit of his firm's client, Styling Technology Corporation ("Styling") in 1996. Styling is a publicly-traded wholesaler of beauty care products. Respondent conducted audits for Styling for the years ending December 31, 1997, and December 31, 1998. During those audit periods respondent served as audit manager. Respondent's engagement partner in charge of those audits was Jay S. Ozer, respondent's supervisor. During the 1997 and 1998 audit periods Styling acquired several companies. Respondent also participated in the preparation of Styling's 10-Q filings for the second quarter of 1999. In April 1999, Styling hired respondent as Vice President of Accounting and Finance. Respondent was one of four Arthur Andersen employees that left that firm and accepted positions with Styling. At Styling respondent managed a five person audit team.

4. In December 2003, the Securities and Exchange Commission ("Commission") filed a complaint against respondent for improper accounting practices. The complaint alleged that respondent engaged in improper accounting practices during the time he was employed by Arthur Andersen when he audited that firm's client, Styling. The complaint alleged that respondent encountered numerous red flags that should have caused him to become aware of significant financial problems at Styling. The complaint further alleged that respondent's failure caused the Arthur Andersen firm to render an unqualified audit report on Styling's 1998 financial statements, which was the result of falsely representing that the audit had been conducted in accordance with generally accepted auditing standards. The complaint also alleged that respondent subjected his license to discipline for acts committed by respondent after he became an employee of Styling. Anticipating the proceedings against him, respondent tendered to the Commission an offer of settlement. His offer was accepted by the Commission. Accordingly and pursuant to that settlement, on May 7, 2004, the U.S. District Court for the District of Columbia entered a final judgment by consent against respondent. The judgment permanently enjoined respondent from violating Section 17(a) of the Securities Act of 1933 and other provisions, and imposed a \$30,000.00 civil penalty. The settlement included respondent's consent to the entry of the Order against him, but without respondent admitting or denying the allegations contained in the Commission's complaint.

5. On May 11, 2004, respondent consented to the entry of an Administrative Order issued by the Commission. As in his consent to the entry of the District Court's Order, respondent's consent to the entry of the Commission's Order was given without respondent admitting or denying the findings contained in the Commission's Order.

6. The allegations in the complaint filed by the Commission against respondent were not litigated. The matter entitled: In the Matter of Bradely J. Schmidt, CPA, Administrative Proceeding File No. 3-11486, was resolved by settlement. The Administrative Order issued pursuant to the settlement was not the result of findings of facts in support of those allegations.

7. Respondent denies complicity with Styling's owner and officers in their fraudulent practices. He asserts that he would have done things differently had he known about the improper practices. He asserts that his audit findings were based on false information provided to him by management. They reported to him extensive sales of their products when in fact the inventory had not been sold, a practice known as: "Bill and Hold". Some Bill and Hold operations are legitimate. The sale actually takes place but the seller agrees to hold the product for the customer in its warehouse. When done fraudulently it is a revenue enhancing practice based on false sales reports. After reporting the nonexistent sales, Styling's management then caused the unsold products to be shipped and stored in warehouses. Respondent became aware of Styling's use of this practice. He learned about some, but not all, of the Bill and Hold orders. Whether the Bill and Hold practice is legitimate or fraudulent is often unclear. Respondent asserts that he became aware of and reported to the Styling Board of Directors the Bill and Hold practice. It was respondent's mistaken belief that the revenues prospectively generated through write-offs, resulting from the Bill and Hold practice amounted to only several hundred thousand dollars. It was not until later that respondent learned the amount involved was several million dollars. He acknowledges he should have been more skeptical and circumspect. He realizes he should have probed deeper to uncover the false reporting practices of management. Respondent asserts that he employed generally accepted auditing practices, but now concedes that he was naive and he should have asked "harder questions." The complexity of respondent's undertakings was enhanced by Styling acquiring four businesses, each requiring its own separate audit. Styling was going public which required additional involvement by respondent and his team. Also Styling is a high profile company in the process of expanding.

8. The evidence does not show that respondent knowingly participated in Styling's fraudulent practices. The evidence does show however, that if he had extended his efforts and followed through in his audit inquiries, he would not have been caught unaware of the extent of the fraudulent practices and he would not have been unaware of the extensive dollar or tax credit amount involved in the fraudulent practices.

Circumstances in Mitigation

9. Respondent has been a licensed Certified Public Accountant since 1995. Prior to this incident he has never had a complaint filed against him and he has not been cited for the violation of any law or regulation.

LEGAL CONCLUSIONS

1. Business and Professions Code section 5109, provides:

The expiration, cancellation, forfeiture, or suspension of a license, practice, privilege, or other authority to practice public accountancy by operation of law or by order or decision of the board or a court of law, or the voluntary surrender of a license by a licensee shall not deprive the board of jurisdiction to

commence or proceed with any investigation of or action or disciplinary proceeding against the licensee, or to render a decision suspending or revoking the license.

2. Respondent's license was renewed in an inactive status and was scheduled to expire on March 31, 2005. Section 5109 provides that the Board shall retain jurisdiction over respondent's license for disciplinary purposes even if the license is allowed to expire before the disciplinary proceeding is concluded.

3. Business and Professions Code section 5100 (g), provides:

After notice and hearing the board may revoke, suspend, or refuse to renew any permit or certificate granted under Article 4 (commencing with Section 5070) and Article 5 (commencing with Section 5080), or may censure the holder of that permit or certificate for unprofessional conduct that includes, but is not limited to, one or any combination of the following causes:

...

(g) Willful violation of this chapter or any rule or regulation promulgated by the board under the authority granted under this chapter.

4. Respondent did not willfully violate the rules and regulations governing the practice of accounting. He did not violate subsection (g). Nevertheless, respondent's license is subject to discipline including revocation for unprofessional conduct. Respondent recklessly failed to ensure that his audit team follow adequate audit procedures. His failures caused Arthur Anderson to render an unqualified audit report on Styling's 1998 financial statements. Further, respondent knew or was reckless in not knowing that Styling's 1999 second quarter Form 10-Q contained false and misleading sales reports.

5. Business and Professions Code section 5100 (h), provides:

After notice and hearing the board may revoke, suspend, or refuse to renew any permit or certificate granted under Article 4 (commencing with Section 5070) and Article 5 (commencing with Section 5080), or may censure the holder of that permit or certificate for unprofessional conduct that includes, but is not limited to, one or any combination of the following causes:

(h) Suspension or revocation of the right to practice before any governmental body or agency.

(l) The imposition of any discipline, penalty, or sanction on a registered public accounting firm or any associated person of

such firm, or both, or on any other holder of a permit, certificate, license, or other authority to practice in this state, by the Public Company Accounting Oversight Board or the United States Securities and Exchange Commission, or their designees under the Sarbanes-Oxley Act of 2002 or other federal legislation.

6. The complaint filed by the Commission against respondent culminated in a settlement agreement. The settlement provided for the issuance of an Order by the Commission wherein the respondent was suspended from appearing or practicing before the Commission as an accountant. Cause exists to discipline respondent's license under Business and Professions Code section 5100 subdivisions (h) and (l).

7. In cases of this nature a very fine line exists between innocent good-faith efforts, based on generally accepted auditing practices, and those auditing practices which fail to heed indicators of irregularities which inevitably, yet unintentionally, facilitate corporate fraud. Respondent's professional responsibility included adjusting his effort commensurate with the complexity of the tasks at hand. In this case Styling had acquired four businesses, each requiring its own separate audit. Styling was going public which required extensive involvement by respondent and his team. All such factors intensify the difficulty in obtaining an accurate view of company records. Respondent was obligated to Styling to exercise the highest level of professional skill. His efforts were not commensurate with the challenge placed before him as Styling's Vice President of Accounting and Finance.

ORDER

Certified Public Accountant Certificate Number 69363 issued to respondent is revoked provided however: The revocation is stayed and respondent is placed on probation for three years upon the following terms and conditions:

1. Respondent shall obey all federal, California, other states' and local laws, including those rules relating to the practice of public accountancy in California.
2. Respondent shall submit, within 10 days of completion of the quarter, written reports to the Board on a form obtained from the Board. The respondent shall submit, under penalty of perjury, such other written reports, declarations, and verification of actions as are required. These declarations shall contain statements relative to respondent's compliance with all the terms and conditions of probation. Respondent shall immediately execute all release of information forms as may be required by the Board or its representatives.

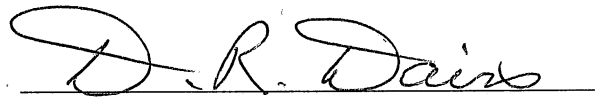
3. Respondent shall, during the period of probation, appear in person at interviews/meetings as directed by the Board or its designated representatives, provided such notification is accomplished in a timely manner.
4. Respondent shall fully comply with the terms and conditions of the probation imposed by the Board and shall cooperate fully with representatives of the California Board of Accountancy in its monitoring and investigation of the respondent's compliance with probation terms and conditions.
5. Respondent shall be subject to, and shall permit, a practice investigation of the respondent's professional practice. Such a practice investigation shall be conducted by representatives of the Board, provided notification of such review is accomplished in a timely manner.
6. Respondent shall comply with all final orders resulting from citations issued by the California Board of Accountancy.
7. In the event respondent should leave California to reside or practice outside this state, respondent must notify the Board in writing of the dates of departure and return. Periods of non-California residency or practice outside the state shall not apply to reduction of the probationary period, or of any suspension. No obligation imposed herein, including requirements to file written reports, reimburse the Board costs, and make restitution to consumers, shall be suspended or otherwise affected by such periods of out-of-state residency or practice except at the written direction of the Board.
8. If respondent violates probation in any respect, the Board, after giving respondent notice and an opportunity to be heard, may revoke probation and carry out the disciplinary order that was stayed. If an accusation or a petition to revoke probation is filed against respondent during probation, the Board shall have continuing jurisdiction until the matter is final, and the period of probation shall be extended until the matter is final.
9. Upon successful completion of probation, respondent's license will be fully restored.
10. Within thirty days of the effective date of this decision, respondent shall submit to the Board or its designee for its prior approval a plan of practice that shall be monitored by another CPA or PA who provides periodic reports to the Board or its designee. Respondent shall pay all costs for such monitoring.
11. Respondent shall complete professional education courses as specified by the Board or its designee at the time of respondent's first probation appearance. The professional education courses shall be completed within a period of time designated and specified in writing by the Board or its designee, which time frame shall be

incorporated as a condition of this probation. This shall not be in addition to continuing education requirements for relicensing.

12. Failure to satisfactorily complete the required courses as scheduled or failure to complete same no later than 100 days prior to the termination of probation shall constitute a violation of probation.

13. Respondent shall at all times maintain an active license status with the Board, including during any period of suspension. If the license is expired at the time the Board's decision becomes effective, the license must be renewed within 30 days of the effective date of the decision.

Dated: May 3, 2005

A handwritten signature in cursive script, reading "D. R. Davis", written over a horizontal line.

DENNY R. DAVIS

Administrative Law Judge

Office of Administrative Hearings

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of the State of California
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9 **BEFORE THE**
10 **CALIFORNIA BOARD OF ACCOUNTANCY**
11 **DEPARTMENT OF CONSUMER AFFAIRS**
STATE OF CALIFORNIA

12 In the Matter of the Accusation Against:

Case No. AC-2005-1

13 BRADLEY JAMES SCHMIDT
4591 East Calle Redonda
14 Phoenix, AZ 85018

ACCUSATION

15 Certified Public Accountant Certificate No.
69363

16
17 Respondent.

18 Complainant alleges:

19 **PARTIES**

20 1. Carol Sigmann (Complainant) brings this Accusation solely in her official
21 capacity as the Executive Officer of the California Board of Accountancy (hereinafter "Board"),
22 Department of Consumer Affairs.

23 2. On or about July 21, 1995, the Board issued Certified Public Accountant
24 Certificate Number 69363 to BRADLEY JAMES SCHMIDT (Respondent). The Certificate was
25 renewed in an active status except from April 1, 1999, through April 30, 2000, and from April 1,
26 2001, through February 12, 2002, when it was in a delinquent status for nonpayment of renewal
27 fees.

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1 3. Effective February 13, 2002, the Certificate was renewed in an inactive
2 status through March 31, 2003. The Certificate was expired from April 1, 2003, through
3 September 3, 2003, and on September 4, 2003, was renewed in an inactive status through March
4 31, 2005.

5 **STATUTES AND PROFESSIONAL STANDARDS**

6 4. Section 5109 of the Business and Professions Code (hereinafter "Code")
7 states:

8 "The expiration, cancellation, forfeiture, or suspension of a license by operation of
9 law or by order or decision of the board or a court of law, or the voluntary surrender of a license
10 by a licensee shall not deprive the board of jurisdiction to proceed with any investigation of or
11 action or disciplinary proceeding against the licensee, or to render a decision suspending or
12 revoking the license."

13 5. Section 5100 of the Code states, in pertinent part:

14 "After notice and hearing the board may revoke, suspend or refuse to renew any
15 permit or certificate granted under Article 4 (commencing with Section 5070) and Article 5
16 (commencing with Section 5080), or may censure the holder of that permit or certificate for
17 unprofessional conduct which includes, but is not limited to, one or any combination of the
18 following causes:

19 "(g) Willful violation of the Accountancy Act or any rule or regulation
20 promulgated by the board."

21 "(h) Suspension or revocation of the right to practice before any government body
22 or agency . . ."

23 "(i) The imposition of any discipline, penalty, or sanction on a registered public
24 accounting firm or any associated person of such firm, or both, or on any other holder of a
25 permit, certificate, license, or other authority to practice in this state, by the Public Company
26 Accounting Oversight Board or the United States Securities and Exchange Commission, or their
27 designees under the Sarbanes-Oxley Act of 2002 or other federal legislation."

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FIRST CAUSE FOR DISCIPLINE

Suspension of Right to Practice Before a Governmental Body or Agency

6. Respondent is subject to disciplinary action under section 5100(h) of the Code in that Respondent has been suspended from the right to practice or appear before the United States Securities and Exchange Commission. The circumstances are as follows:

A. On May 11, 2004, in a case entitled *In the Matter of Bradley J. Schmidt, CPA, Administrative Proceeding File No. 3-11486*, the Securities and Exchange Commission ("Commission") issued an Order Instituting Public Administrative Proceedings Pursuant to Rule 102(e)(3) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order").¹ Pursuant to the Order, Respondent was suspended from appearing or practicing before the Commission as an accountant. After five years, Respondent may request that the Commission consider his reinstatement subject to certain conditions. The Order was based on the following action:

In or about December 2003, the Commission filed a complaint in the United States District Court for the District of Columbia against Respondent alleging that Respondent engaged in improper professional conduct within the meaning of Rule 102(e)(3) in connection with Arthur Andersen's audits of Styling Technology Corporation ("Styling") for the years ended December 31, 1997, and December 31, 1998, and in connection with Styling's 10-Q filings for the second quarter of 1999. The complaint alleged that, in the course of the 1998 year-end audit of Styling, Respondent encountered numerous red flags that should have alerted him to significant financial problems at the company, yet recklessly failed to ensure that the audit team follow basic audit procedures in its examination of the company. The complaint alleged that the Respondent and the audit partner then caused Arthur Andersen to render an unqualified audit report on

1. Rule 102(e)(3)(i) provides, in relevant part, that the Commission, "with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder."

1 Styling's 1998 financial statements, falsely representing that the Styling audit had been conducted
2 in accordance with generally accepted auditing standards and that Styling had reported its
3 financial condition and results of operations in conformity with generally accepted accounting
4 principles. The complaint further alleged that Respondent, while serving as Styling's vice
5 president of financial reporting, participated in the preparation of the company's 1999 second
6 quarter Form 10-Q, which he knew or was reckless in not knowing contained false and misleading
7 statements concerning Styling's sales during the quarter.

8 On May 7, 2004, the court entered an order permanently enjoining Respondent, by
9 consent, from violating various securities laws and regulations. In addition, Respondent was
10 ordered to pay a civil penalty of \$30,000.

11 **SECOND CAUSE FOR DISCIPLINE**

12 **The Imposition of Discipline, Penalty or Sanction by the**
13 **U.S. Securities and Exchange Commission**

14 7. Respondent is subject to disciplinary action under section 5100(l) of the Code in
15 that Respondent has been disciplined by the United States Securities and Exchange Commission,
16 as more fully set forth in paragraph 6(A).

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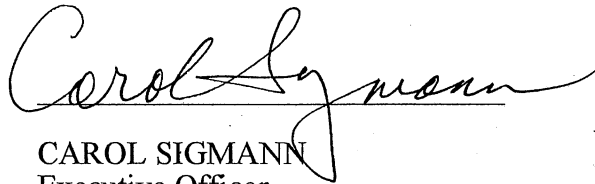
1 **PRAYER**

2 WHEREFORE, Complainant requests that a hearing be held on the matters herein
3 alleged, and that following the hearing, the California Board of Accountancy issue a decision:

4 1. Revoking, suspending or otherwise imposing discipline upon Certified Public
5 Accountant Certificate Number 69363, issued to BRADLEY JAMES SCHMIDT;

6 2. Taking such other and further action as may be deemed proper.

7
8 DATED: September 24, 2004

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11 CAROL SIGMANN
12 Executive Officer
13 California Board of Accountancy
14 Department of Consumer Affairs
15 State of California
16 Complainant
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